



**CITY OF SCOTTSDALE  
AUDIT COMMITTEE**

**MONDAY, NOVEMBER 24, 2008**

**CITY HALL, KIVA CONFERENCE ROOM  
3939 NORTH DRINKWATER BLVD  
SCOTTSDALE, AZ 85251**

**PRESENT:** W.J. "Jim" Lane, Chair  
Wayne Ecton, Councilman  
Ron McCullagh, Councilman

**STAFF:** Brent Stockwell, City Auditor's Office  
Joyce Gilbride, City Auditor's Office  
Susan English, City Auditor's Office  
Neal Shearer, Assistant City Manager  
Craig Clifford, Financial Services  
Richard Chess, Financial Services  
Paula Novacek, Financial Services  
La Verne Parker Diggs, Human Resources  
Bernadette LaMazza, Human Resources  
Michael Clack, Planning and Development Services

**GUESTS:** Carter Smitherman, Cronstrom, Osuch & Co.

**Call to Order/Roll Call**

Chairman Lane called the Audit Committee meeting to order at 3:00 p.m.

Roll call was taken confirming the presence of Committee Members as noted above.

**1. Approval of Minutes from the Regular Meeting on October 27, 2008**

Committee Member Ecton made a motion to approve the October 27, 2008 minutes. Committee Member McCullagh seconded the motion. The minutes were approved by a unanimous vote of three (3) to zero (0).

**2. Discussion with the City's external auditors Cronstrom, Osuch & Company on the results of the annual audit, the 2008 Comprehensive Annual Financial Report (CAFR), Management Letter, and single Audit Report**

Carter Smitherman provided the Committee with the Management Letter and Single Audit Report. In addition, he provided a letter to Management and the Committee, as now required by law, discussing issues regarding the audit.

The management letter had one recommendation having to do with procurement. Quotes were not obtained for two out of ten purchases in required range; however, subsequent to the issuance of this letter and upon further investigation, documentation was provided that resolved these two particular instances.

In regard to the Single Audit Report, internal controls are in compliance with government auditing standards, and there were no findings reported under those standards. In response to Chairman Lane, Mr. Smitherman explained while the audit does review the City's internal controls; no opinions are rendered on them. Key internal controls are tested in order to provide assurance that they can be relied upon during the audit.

Chairman Lane asked to what extent City staff is involved in this audit. Mr. Smitherman clarified his firm does the entire financial review, including understanding of internal controls, testing of internal controls, and the substantive tests of those controls, which establishes the level of testing in the audit.

Mr. Smitherman said the Single Audit Report does contain an unqualified opinion on compliance with federal requirements of major programs, and the audit revealed no findings to report.

The CAFR includes all information prepared by management, the auditors' opinion, management's discussion and analysis, the financial statements, and the notes to the financial statements with all required disclosures. Mr. Smitherman pointed out that the report contains an unqualified opinion that the financial statements are materially stated. The audit went very smoothly, and staff did a tremendous job in closing out the year and getting all the necessary information ready for the audit.

In response to an inquiry by Chairman Lane, Mr. Smitherman stated his firm has been performing the City's external audit services for approximately eight years.

Financial Services General Manager Craig Clifford said this would be placed on a consent agenda for City Council review in order for staff to follow through and get the reports out to other agencies, such as the bond rating agencies that utilize the City's audited financial statements.

**3. Staff update and discussion regarding the sale of City assets on the internet including past audit work, actions taken by management, and current practices**

Acting City Auditor Brent Stockwell gave a brief background regarding this item, noting prior audit work has been done on high-risk, non-capital tangible property. The audit in 2005 included recommendations regarding steps the Financial Services general

manager could take. Chairman Lane asked if those recommendations were implemented. Mr. Clifford clarified Financial Services has made no changes to Regulation 226 as there is no need to make any changes to the procedures and the controls are adequate. The process is currently being enhanced by creating a formal transmittal form for surplus property from the department to Procurement, acknowledging what they are transmitting and receipt of the property. Financial Services is following up on feedback with the departments as far as the inventory process for these high-risk assets. The AR places the responsibility with the department to maintain the lists. Surplus items are no longer sold directly to employees; however, they can buy items if they go to the City's auction.

Chairman Lane asked whether policy has been violated in this regard. Chief Development Officer Michael Clack said there was some outdated equipment sold that was not disposed of through the procurement process. Mr. Clifford said if there was a violation, it was that the employee took what was deemed surplus and sold it. Chairman Lane asked if there is any indication that this is a continuing situation, and Mr. Clifford indicated it is not. He assured the Committee that adequate procedures and controls are in place.

Chairman Lane asked who determines that property should be turned over to Procurement as a surplus item. Mr. Clifford said the manager of each department makes that decision.

Committee Member Ecton stated many of these questions could only be answered after a full-blown audit has been conducted. Mr. Stockwell said the audit work that was completed in 2005 indicated that the information needed to conduct an audit of the high-risk, non-capital tangible items was not present. An additional audit would have to be scheduled in order to do any follow-up work.

Committee Member Ecton said in this type of situation, the City must decide if it is worth the time and the money to try and track everything that could end up on a high-risk list.

Chairman Lane said the City should maintain an environment that does not easily allow this type of activity, and training and education on City policy is important. Mr. Clifford said the City currently has Surplus Regulations in the Procurement Code as well as an AR regarding this issue, and Human Resources disciplinary provisions are in place. It is a matter of continually educating employees to ensure they do the right thing and behave ethically.

#### **4. Staff update, discussion, and possible recommendation to the City Council regarding recruitment process for the position of City Auditor**

Human Resources General Manager La Verne Parker Diggs presented the Committee with materials concerning the recruitment for the City Auditor position, including a City Council report and a resolution that would authorize the Audit Committee to serve as the search committee for that position. The recruitment brochure includes information about the City and its mission, as well as the specifications for an ideal candidate. The brochure states that the compensation for this position is highly competitive rather than including a set salary, and lists all City benefits. A list of web sites and organizations where the ad will be placed was provided to the Committee, along with the job

description that will be advertised. Ms. Parker Diggs discussed the search plan; the intention is to identify the preferred candidate by March 25, 2009, if the advertisement begins by December 11, 2008.

Committee Member McCullagh expressed concern regarding the seven-year requirement for management at public agencies. He stated he is not sure this position would require an applicant to have conducted or managed audits in public agencies. In addition, he stated he does not believe the requirement for a master's degree in accounting, finance, business, or public administration is necessary; a bachelor's degree with a CPA accreditation would probably be sufficient. He indicated the preference for demonstrated experience in working with elected and appointed officials could narrow the field too much.

Chairman Lane agreed that the seven-year requirement of directing the auditing affairs of a public entity may not be necessary, especially if the Committee is looking at the possibility of including private sector candidates involved in public accounting or auditing. He suggested deleting that requirement from the job description. He stated he believes a master's degree is now required for a CPA; however, the emphasis should be on the certifications.

Committee Member Ecton said the person recruited for this position should have the necessary experience and background, and that should be discussed thoroughly. The master's degree requirement would ensure the candidate has had additional training in pertinent areas.

Committee Member McCullagh said he does not have an objection to giving priority to a candidate who has experience in the public sector or has a master's degree; however, if those are included as requirements in the job description, it will preclude many good candidates.

Chairman Lane agreed he does not want to exclude a candidate who does not have a master's degree or public sector experience. He indicated he believes candidates from the private sector should be considered. The job description should ask for auditing and management experience, along with the proper credentials.

Ms. Parker Diggs said the language of the job description could be modified to be more inclusive.

The Committee agreed to make the job description more inclusive by reducing the language that refers to working for public entities and the master's degree requirement. The preference for working with elected and appointed public officials will be changed to any board or committee, public or private.

Committee Member Ecton said he supported the recommended schedule, and would like to have these adjustments made as soon as possible in order to keep to it. He asked if it would be necessary to have another Committee meeting in order to approve any final changes. The Committee agreed that Ms. Parker Diggs should make the necessary changes and go forward with the search; further Committee approval is not necessary.

The City Council report will be presented to the Council on December 2, 2008, and the recruitment process will begin on December 11, 2008. The brochures will be distributed on December 15, 2008.

Ms. Parker Diggs stated that Human Resources would identify candidates who meet the requirements and forward those applications to the Committee.

## **5. Staff update and discussion regarding status of current audits and office budget**

Mr. Stockwell provided the Committee with an audit status update and budget summary. There are currently seven audits in progress, and those reports will be issued from January through March 2009. The audits remain on schedule per the approved audit plan. The next three audits to start will be Water System Security, the Use of Purchase Orders, and In Lieu Parking.

Mr. Stockwell indicated the Audit Department's move to their new facilities went well.

Mr. Stockwell explained that Mr. Clifford had suggested that the Committee be updated on the department's proposed budget reductions. The move to the new facility has had a big impact on the current budget, and is 18.9 percent of the total budget. The Audit Department is a relatively small area, with a total budget of just over \$900,000. Only 3.4 percent of the budget is discretionary, and City Code requires some of the items that are paid for with these funds, such as peer review and continuing professional education for staff. Personnel costs comprise 86.4 percent of the fiscal year 2008/09 budget. The department currently has eight full time employees, and it is important to note that the number of staff in the City Auditor's Office has remained the same for the past 11 years with no increases in staffing since fiscal year 1997/98. The only way to reach the 10 percent reduction goal is to eliminate one position, and Mr. Stockwell indicated his preference for attaining that goal is through attrition.

Committee Member McCullagh asked if the Audit Department spent the funds allotted for the move. Mr. Stockwell said almost all of those funds have been spent. Committee Member McCullagh said part of the reason there is a reduction in the FY 2009/10 budget is because there is no longer a need for it. He indicated the reductions shown are misleading because since the department has been moved those items would not be budgeted for anyway.

Committee Member Ecton said since the only way to meet the 10 percent budget reduction goal is to eliminate an employee, then that should be a discussion the Committee participates in. The number of audits performed per year will be affected, and could possibly expose the City to problems.

Chairman Lane said that he feels that audits are inherently valuable to the organization, and that the Committee should be prepared to make a recommendation on whether or not to eliminate a position within the department in order to meet the budget.

Committee Member McCullagh noted the report says the cost to the department of eliminating one employee is three medium-sized audits, implying the department does 21 audits a year. Mr. Stockwell said that would be based on which position was actually

eliminated, and that the three audit reductions could occur if an auditor or senior auditor position was eliminated.

Assistant City Manager Neal Shearer commented that City management recognizes that the City Auditor's Office has a direct reporting relationship to the City Council through a charter position. The fiscal year 2009/10 budget will put everything in context, and these decisions can be made after the complete picture is clear.

In regard to an inquiry by Chairman Lane, Mr. Stockwell said in the five-month period he has been Acting City Auditor, the Audit Department has finished nine projects, with a projected total of 16 audits completed by March. In the previous fiscal year there were 11 audits completed. Chairman Lane said he believes productivity has improved.

#### **6. Discussion of agenda items for next Audit Committee meeting**

Mr. Stockwell presented the Committee with items anticipated for inclusion on the next agenda. The next meeting will be held Monday, January 26, 2009, at 3:00 p.m. Three audit reports will be brought to the Committee at that time, as well as a review of the applications received for the position of City Auditor. A special meeting may be necessary to cover all of these items; however, there will be no committee meeting in either December 2008 or July 2009.

#### **Public Comment**

None

#### **Adjournment**

With no further business to discuss, the Audit Committee meeting adjourned at 4:33 p.m.